

CITY OF ROCHESTER, MINNESOTA
NOTES TO THE FINANCIAL STATEMENTS
December 31, 2001

NOTE 1: Summary of Significant Accounting Policies

The financial statements of the City of Rochester, Minnesota have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The more significant of the City's accounting policies are described below.

A. Reporting Entity

The City of Rochester, Minnesota (the City) is a municipal corporation, incorporated under the laws of the State of Minnesota, and governed under a charter adopted in 1904.

Component units are legally separate entities which are fiscally dependent on the primary government or for which the primary government is financially accountable. As of December 31, 2001, there were no entities that met the requirements to be considered a component unit of the City.

B. Fund Accounting

The City uses funds and account groups to report on its financial position and the results of its operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

A fund is a separate accounting entity with a self-balancing set of accounts. An account group, on the other hand, is a financial reporting device designed to provide accountability for certain assets and liabilities that are not recorded in the funds because they do not directly affect net expendable available financial resources.

Funds are classified into three categories: governmental, proprietary and fiduciary. Each category, in turn, is divided into separate "fund types."

Governmental funds are used to account for all or most of the City's general activities, including the collection and disbursement of earmarked monies (Special Revenue Funds), the acquisition or construction of general fixed assets (Capital Projects Funds), and the servicing of general long-term debt (Debt Service Funds). The General Fund is used to account for all activities of the general government not accounted for in some other fund.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 1: Summary of Significant Accounting Policies (Continued)

B. Fund Accounting (Continued)

Proprietary funds are used to account for activities similar to those found in the private sector, where the determination of net income is necessary or useful to sound financial administration. Goods or services from such activities can be provided either to outside parties (Enterprise Funds) or to other departments or agencies primarily within the City (Internal Service Funds.)

Fiduciary funds are used to account for assets held on behalf of outside parties, including other governments, or on behalf of other funds within the City. When these assets are held under the terms of a formal trust agreement, a nonexpendable trust fund or an expendable trust fund is used. The terms "nonexpendable" and "expendable" refer to whether or not the City is under an obligation to maintain the trust principal. The City's trust fund is classified as "expendable" and is accounted for in essentially the same manner as governmental funds.

C. Basis of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds and expendable trust funds are accounted for on a spending or "financial flow" measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets.

All proprietary funds are accounted for on a cost of services or "capital maintenance" measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the balance sheet. Fund equity is segregated into contributed capital and retained earnings components. Proprietary fund-type operating statements present increases and decreases in net total assets. With respect to proprietary activities, the City has elected to apply all Governmental Accounting Standards Board (GASB) pronouncements as well as Financial Accounting and Standards Board pronouncements and Accounting Principles Board Opinions, issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

The modified accrual basis of accounting is used by all governmental fund types and expendable trust funds. Under the modified accrual basis of accounting, revenues

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 1: Summary of Significant Accounting Policies (Continued)

C. Basis of Accounting (Continued)

are recognized when susceptible to accrual (i.e., when they become both measurable and available). "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period.

The City considers property taxes as available if they are collected within 60 days after year end. Expenditures are recorded when the related fund liability is incurred. Principal and interest on general long-term debt are recorded as fund liabilities when due. Inventory items are considered expenditures when consumed.

Those revenues susceptible to accrual are taxes, special assessments, intergovernmental revenues, charges for services and interest earnings. Licenses and permits, fines and forfeits, and miscellaneous revenues are not susceptible to accrual because generally they are not measurable until received in cash.

The City also reports deferred revenue on its combined balance sheet for its governmental funds. Deferred revenues arise when a potential revenue does not meet both the "measurable" and "available" criteria for recognition in the current period. Deferred revenues also arise when resources are received by the City before it has a legal claim to them, as when grant monies are received prior to the incurrence of qualifying expenditures. In subsequent periods, when both revenue recognition criteria are met, or when the City has a legal claim to the resources, the liability for deferred revenue is removed from the combined balance sheet and revenue is recognized.

The accrual basis of accounting is utilized by the proprietary fund types. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

D. Budgets and Budgetary Accounting

Budgets are adopted on a basis consistent with generally accepted accounting principles. Annual appropriated budgets are legally adopted by Council resolution for the General and Special Revenue Funds.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 1: Summary of Significant Accounting Policies (Continued)

D. Budgets and Budgetary Accounting (Continued)

Formal budgetary integration is employed as a management control device during the year for the General Fund and Special Revenue Funds. Formal budgetary integration is not employed for the Debt Service Funds because effective budgetary control is alternately achieved through general obligation bond indenture provisions. Budgetary control for the Capital Project Funds is based on a project completion time cycle rather than an annual basis, therefore budgetary comparisons on an annual basis would not present meaningful information.

Encumbrances represent purchase orders, contracts and other commitments for the expenditure of funds. Encumbrances are not considered the equivalent of expenditures, therefore the encumbrances outstanding at year end are reported as a reserved portion of the fund balance in the General, Special Revenue and Capital Project Funds.

The City follows these legal compliance procedures in establishing the budgetary data reflected in the financial statements:

1. The City Administrator submits a proposed operating budget to the City Council prior to the end of each year for the fiscal year commencing the following January 1. The operating budget includes proposed expenditures and means of financing them.
2. Public hearings are conducted to obtain taxpayer comments.
3. Prior to December 28, the budget is legally enacted through the passage of a budget resolution.
4. Any changes to the budget at the functional level must be by formal resolution of the City Council. Generally, budget amendments result in utilization of contingency appropriations and do not alter the total expenditure budget of the City. Monitoring of budgets is maintained at the department level by departments or divisions. However, expenditures in excess of the departmental budget require administrative approval.
5. All budgeted appropriations lapse at the end of the fiscal year. The expenditures may not legally exceed appropriations at the functional level of control presented in the financial statements at Form A-3.

The budget presentations for the current year are as originally adopted, or as amended by utilizing contingency appropriation transfers. There were no material supplemental appropriations during the year.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 1: Summary of Significant Accounting Policies (Continued)

E. Cash and Investments

Cash balances from all funds are combined and invested to the extent available in authorized investments. Earnings from such investments are allocated to respective funds on the basis of applicable cash balance participation by each fund.

Investments are stated at fair value, based upon quoted market prices at the reporting date.

Cash and cash equivalents for purposes of the general purpose financial statements includes amounts in demand deposits as well as short-term investments with a maturity date within three months of the date acquired by the City.

F. Inventory

The materials and supplies inventories are valued at moving average cost on a first-in, first-out basis. Fossil fuel inventories in the Enterprise Funds are valued at the lower of cost on a last-in, first-out basis, or market. Purchases are reported as expenditures when the inventory items are consumed (consumption method).

G. Property, Plant and Equipment

Property, plant and equipment and construction work in process are stated at cost except for assets contributed or donated to the City, which are stated at their estimated fair market value on the date received. Interest incurred during the construction phase is included in the capitalized value of the asset constructed, net of interest earned on the invested debt proceeds over the same period.

General Fixed Assets:

Property, plant and equipment including construction work in process are recorded as expenditures of the General, Special Revenue, and Capital Project Funds at the time of their acquisition. Such assets are then capitalized in the General Fixed Assets Account Group. Public domain ("infrastructure") general fixed assets consisting of certain improvements other than buildings, including roads, bridges, curbs and gutters, streets and sidewalks, drainage systems and lighting systems are capitalized along with other general fixed assets. No depreciation is provided for these assets.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 1: Summary of Significant Accounting Policies (Continued)

G. Property, Plant and Equipment (Continued)

Proprietary Funds:

Property, plant and equipment are capitalized when acquired, and depreciation is provided using the straight-line method applied over the following estimated useful lives of the assets.

	<u>Useful Life</u> <u>in Years</u>
Buildings and Improvements	10 - 50
Other Improvements	5 - 75
Machinery and Equipment	2 - 25

H. Property Taxes

Property tax levies are set by the City Council in December of each year and are certified to Olmsted County for collection in the following year. In Minnesota, counties act as collection agents for all property taxes. The County spreads all levies over taxable property. Such taxes become a lien on January 1, of the following year, and are recorded as receivables by the City at that date. Revenues from property taxes are accrued and recognized in the year collectible, net of delinquencies.

Real property taxes may be paid by taxpayers in two equal installments on May 15 and October 15. Personal property taxes may be paid on February 28 and June 30. The County provides tax settlements to cities and other taxing districts normally during the months of January, June and December.

Taxes which remain unpaid at December 31 are classified as delinquent taxes receivable, net of an allowance for uncollectible taxes currently estimated at 3.0% of the outstanding balance. The net amount of delinquent taxes receivable are fully offset by deferred revenue in the Governmental Fund Types because they are not known to be available to finance current expenditures.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 1: Summary of Significant Accounting Policies (Continued)

I. Special Assessments

Assessments are levied at various times upon City Council resolution for property owner improvements made by the City. Generally, assessment collections are deferred over periods ranging from one to fifteen years with interest charges of 7.5%. Revenue from these assessments is recognized as the annual installments become collectible. Annual installments not collected as of each December 31 are classified as delinquent assessments receivable. Delinquent assessments receivable are carried net of an allowance for uncollectible assessments estimated at 3.0% of the outstanding balance. The net amount of delinquent assessments receivable are fully offset by deferred revenue in the Governmental Fund Types because they are not known to be available to finance current expenditures.

J. Utility Connection Charges

The City enters into utility connection agreements with certain residential property owners that elect to convert to City utilities. Under these agreements, property owners may elect to pay connection charges in full or make payments to the City as special assessments over ten years as reimbursement for City made improvements. Utility connection charges are based on a flat rate per frontage foot and are limited to a maximum amount per lot based on lot size. Revenue from utility connection agreements is recognized as the charges become collectible.

K. Compensated Absences Benefits

Vacation, sick pay and compensatory overtime are accrued when earned in the Proprietary Fund Types. In Governmental Fund Types, vacation, sick pay and compensatory overtime are recorded as expenditures and accrued as current liabilities during the year they would normally be liquidated with expendable available financial resources. The remainder of the accumulated compensated absences are reported in the General Long-Term debt account group.

The City compensates employees upon termination, for one-third of their unused sick leave, after meeting certain qualifications based upon length of service and a minimum accumulation of hours. The compensation is computed at the employee's rate of pay at the time of termination, and is applied towards the cost of continuing group health and life insurance coverage. The sick leave liability is estimated based on the City's past experience of making termination payments for sick leave.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 1: Summary of Significant Accounting Policies (Continued)

K. Compensated Absences Benefits (Continued)

Unused vacation pay in excess of 40 hours generally expires on each employment anniversary date. Under certain conditions vacation pay will be paid upon termination in good standing. Most employees are also allowed to accumulate compensatory overtime up to a maximum of 80 hours per anniversary period. Certain other employees are allowed to accumulate compensatory overtime up to a maximum of 240 hours.

L. Interfund Transactions

Quasi-external transactions are accounted for as revenues, expenditures or expenses. The in lieu of tax transaction between the General Fund and the Parking, Electric, Water and Sewer Enterprise funds is computed based upon sewer and parking revenues and commodity sales of the electric and water utilities. Transactions that constitute reimbursement to a fund for expenditures or expenses initially made from it that are properly applicable to another fund, are recorded as expenditures or expenses in the reimbursing fund and as a reduction of expenditures or expenses in the fund that is reimbursed.

All other interfund transactions, except quasi-external transactions and reimbursements, are reported as transfers. Nonrecurring or nonroutine permanent transfers of equity are reported as residual equity transfers. All other interfund transfers are reported as operating transfers.

At year end, receivables/payables may result from transactions between individual funds. The short term portion of these receivables/payables are classified on the balance sheet as "due from other funds" or "due to other funds".

The non-current portion of these receivables/payables are classified as "advances to other funds" or "advances from other funds".

Advances between funds are offset by a fund balance reserve account in applicable governmental funds to indicate they are not available for appropriation and are not expendable available financial resources.

M. Comparative Data

Comparative data for the prior year have been presented in certain of the accompanying financial statements in order to provide an understanding of the changes in the City's financial position and operations. However, complete comparative data have not been presented since their inclusion would make the statements unduly complex and difficult to read.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 1: Summary of Significant Accounting Policies (Continued)

M. Comparative Data (Continued)

Certain amounts in the December 31, 2000 totals (Memorandum Only) column have been reclassified to conform with the current year presentation.

N. Concentration of Credit Risk

Financial instruments which expose the City to a concentration of credit risk consist primarily of cash equivalents, accounts receivable and loans receivable. Credit risk associated with cash equivalents is discussed in Note 3.

The City's accounts and loans receivable are concentrated geographically, as for the most part, amounts are due from individuals residing in and businesses located in the City of Rochester.

O. Total Columns on Combined Statements

Total columns on the Combined Statements are captioned Memorandum Only to indicate that they are presented only to facilitate financial analysis. Data in these columns do not present financial position, results of operations, or cash flows in conformity with generally accepted accounting principles. Neither are such data comparable to a consolidation. Interfund eliminations have not been made in the aggregation of this data.

NOTE 2: Stewardship, Compliance and Accountability

For the year ended December 31, 2001, expenditures did not exceed appropriations in any funds.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 3: Cash and Investments

A. Deposits

In accordance with Minnesota Statutes, the City maintains deposits with national banks, insured state banks or thrift institutions as authorized by the City Council.

Balances at December 31, 2001 are as follows:

	<u>Book Balances</u>	<u>Bank Balances</u>
Insured or collateralized by securities held by the City or its agent in the City's name	\$ 7,845,596	\$ 9,042,274
Collateralized by securities held by the pledging Institution's trust department in the City's name	-	-
Uncollateralized or collateralized with securities not in the City's name	-	-
Total	<u>\$ 7,845,596</u>	<u>\$ 9,042,274</u>

Minnesota Statutes requires that all City deposits be insured, secured by surety bond or collateralized, and the market value of collateral pledged must equal 110% of the deposits not covered by insurance or surety bonds.

Authorized collateral includes certain state or local government obligations and legal investments described in Section B. Minnesota Statutes also require that securities pledged as collateral be held in safekeeping by the Treasurer, or in a financial institution other than the institution furnishing the collateral.

B. Investments

The City is authorized by Minnesota Statutes to invest idle funds as follows:

- (a) Direct obligations or obligations guaranteed by the United States or its agencies.
- (b) Shares of investment companies registered under the Federal Investment Company Act of 1940 and whose only investments are in securities described in (a) above.
- (c) General obligations of the State of Minnesota or its municipalities.
- (d) Bankers acceptances of United States banks eligible for purchase by the Federal Reserve System.
- (e) Commercial paper issued by United States corporations or their Canadian subsidiaries, of the highest quality, and maturing in 270 days or less.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 3: Cash and Investments (Continued)

B. Investments (Continued)

- (f) Repurchase agreements with banks that are members of the Federal Reserve System with capitalization exceeding \$10,000,000, a reporting dealer to the Federal Reserve Bank of New York, or certain Minnesota securities broker-dealers.
- (g) Money market funds with institutions that have portfolios consisting exclusively of United States Treasury obligations and Federal Agency issues.

Deposit and investment balances as of December 31, 2001 are as follows:

	Credit Risk Category			Carrying Amount
	1	2	3	
U.S. Governments	\$ 106,940,063	\$	\$	\$ 106,940,063
Commercial Paper	14,967,010			14,967,010
Municipal Bond	13,128,053			13,128,053
Totals	\$ 135,035,126	\$	\$	135,035,126
Investments in money market fund				14,990,311
				150,025,437
Deposits				7,845,596
Change Funds				9,893
Total Deposits and Investments				\$ 157,880,926

A reconciliation of cash and investments as shown on the Combined Balance Sheet follows:

Cash and cash equivalents	\$ 21,569,181
Investments	121,435,571
Restricted assets	14,876,174
	\$ 157,880,926

The City investments are categorized above to give an indication of the level of risk assumed at year end. Category 1 includes investments that are insured or registered or for which the securities are held by the City or its agent in the City's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the City's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in the City's name.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 4: Due From and To Other Governmental Units

Amounts due from other governmental units as of December 31, 2001 are as follows:

<u>Fund Type</u>	<u>Federal Government</u>	<u>State of Minnesota</u>	<u>Olmsted County</u>	<u>Other</u>	<u>Total</u>
General	\$ 33,184	\$ 185,009	\$ 736,937	\$ 72,939	\$ 1,028,069
Special Revenue		359	365,336	26,439	392,134
Capital Project	729,885	2,669,113	669,838		4,068,836
Enterprise		223	12,042		12,265
Totals	<u>\$ 763,069</u>	<u>\$ 2,854,704</u>	<u>\$ 1,784,153</u>	<u>\$ 99,378</u>	<u>\$ 5,501,304</u>

Amounts due to other governmental units as of December 31, 2001 are as follows:

<u>Fund Type</u>	<u>Federal Government</u>	<u>State of Minnesota</u>	<u>Olmsted County</u>	<u>Other</u>	<u>Total</u>
General		\$ 50,179	\$ 159,618	\$ 9,757	\$ 219,554
Special Revenue	\$ 1,415	22,888	57,051	12,785	94,139
Capital Project	1,003	18,362	32,752		52,117
Enterprise		3,227	16,986	265,124	285,337
Internal Service		54			54
Totals	<u>\$ 2,418</u>	<u>\$ 94,710</u>	<u>\$ 266,407</u>	<u>\$ 287,666</u>	<u>\$ 651,201</u>

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 5: Restricted Assets

Restricted assets are deposits held for specifically required purposes and are offset by fund balance reserve accounts. Balances at December 31, 2001, and descriptions are as follows:

General Fund

Civic Music Endowment:

Rochester Area Foundation Endowment	\$ 23,473
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Special Revenue Funds

Memorials for Library Fund use:

Walter Hurlbut Book Fund	33,023
Alice P. Mayo Trust Fund	15,252
Arthur B. Hall Memorial Fund	13,538
Clara Siem Memorial Fund	9,572
V. Huyber Memorial Fund	10,116
Norman D. Wilson Memorial Fund	13,839
Total	<u>95,340</u>

Enterprise Funds

Reserve Account	2,471,688
Construction Account	11,314,844
Escrow Deposits	825,198
Supplemental Pension Reserve	145,631
Total	<u>14,757,361</u>

Total Restricted Assets	<u>\$ 14,876,174</u>
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In 2000, the electric utility issued revenue bonds to fund the construction of a new gas turbine generator and improvements to the electric utility's transmission and distribution system. Provisions of the revenue bonds required that \$2,471,688 of the bond proceeds be deposited in a reserve account to be used to pay bond principal and interest payments if necessary. Under the terms of the revenue bonds, the bond proceeds, net of accrued interest, bond discount, and the reserve requirement, were deposited into a Construction Account to pay all construction-related costs. Any funds remaining in the Construction Account after the payment of these costs must be transferred to a debt service account.

NOTE 6: Property, Plant and Equipment

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

Following is a summary of the various classifications of the Proprietary Fund Type property, plant and equipment and accumulated depreciation as of December 31, 2001:

<u>Enterprise Funds</u>	<u>Amount</u>	<u>Accumulated Depreciation</u>	<u>Net</u>
Land and Land Rights	\$ 5,636,551		\$ 5,636,551
Buildings and Improvements	91,182,695	\$ 43,331,687	47,851,008
Other Improvements	156,757,265	72,705,954	84,051,311
Machinery and Equipment	30,601,599	22,299,466	8,302,133
Construction Work in Process	34,792,043		34,792,043
Totals	<u>\$ 318,970,153</u>	<u>\$ 138,337,107</u>	<u>\$ 180,633,046</u>
 <u>Internal Service Funds</u>			
Machinery and Equipment	<u>\$ 15,940,361</u>	<u>\$ 7,253,107</u>	<u>\$ 8,687,254</u>

A summary of changes in General Fixed Assets for the year ended December 31, 2001 is as follows:

	<u>Balance 1/1/01</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance 12/31/01</u>
Land and Buildings	\$ 129,411,500	\$ 26,771,542		\$ 156,183,042
Other Improvements	184,377,011	7,614,475		191,991,486
Machinery and Equipment	24,193,018	2,641,015	\$ 351,945	26,482,088
	337,981,529	37,027,032	351,945	374,656,616
Construction Work in Process	42,122,425	16,205,992	18,836,712	39,491,705
Totals	<u>\$ 380,103,954</u>	<u>\$ 53,233,024</u>	<u>\$ 19,188,657</u>	<u>\$ 414,148,321</u>

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 7: Long-Term Debt

A summary of long-term debt obligations outstanding at December 31, 2001 is as follows:

	<u>Range of Interest Rates</u>	<u>Final Maturity</u>	<u>Balance 12/31/01</u>
General Obligation Bonds:			
Tax Increment Bonds, Series 1985	6.45-6.5%	2005	\$ 4,775,000
Taxable Tax Increment Bonds			
District 7, Series 1997	5.5%	2024	2,669,380
General Obligation Revenue Bonds:			
Taxable Sales Tax Revenue			
Bond of 2000	6.35%	2010	10,458,673
Temporary Sales Tax Revenue			
Bonds, Series 2000A	4.4%	2003	17,925,000
Wastewater Treatment Plant			
Refunding Bonds, Series 2001A	3.5-4.0%	2011	8,275,000
Revenue Bonds:			
Electric Utility Revenue			
Bonds, Series 2000	4.75-5.25%	2030	36,715,000
Notes Payable:			
Electric Utility	5.56-7.70%	2003	400,000
Airport Hangar - 1998	0%	2008	109,455
Airport Hangar - 1999	0%	2010	147,783
Airport Hangar - 2001	0%	2012	210,049
Total Long-Term Debt			<u>\$ 81,685,340</u>

Current Refunding

During 2001, the City issued \$8,275,000 of General Obligation Revenue Bonds for a current refunding of \$8,250,000 of General Obligation Revenue Refunding Bonds of the Sewer Fund. The refunding was undertaken to reduce total future debt service payments. The excess of the reacquisition price over the net carrying amount of the old debt is being amortized over the life of the new debt. The transaction resulted in an economic gain of \$821,894 and a reduction of \$988,265 in future debt service payments.

General Obligation Tax Increment Bonds

In 1992, an amendment to the Tax Increment Financing plan transferred the balance of Tax Increment Bond, Series 1985, from the Enterprise Funds at the Parking Fund level to the General Long-Term Debt Account Group. The bonds are backed by the full faith, credit and taxing power of the City and are serviced by the Debt Service Funds.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 7: Long-Term Debt (Continued)

General Obligation Taxable Tax Increment Bonds

In 1997, the City authorized Taxable Tax Increment Bonds, District 7 of \$2,768,500. These bonds are structured without fixed principal maturities. Payments are equal to the amount of available tax increments received by the City within the six month period preceding each payment date. These bonds are backed by the full faith, credit, and taxing power of the City and are serviced by the Debt Service Fund.

General Obligation Taxable Sales Tax Revenue Bonds

In 2000, the City authorized Taxable Sales Tax Revenue Bonds of \$10,458,673. These bonds are structured without fixed principal maturities. The bonds are payable from revenues derived from the City's local 0.5% sales and use tax, and are backed by the full faith, credit, and taxing power of the City and are serviced by the Debt Service Fund.

General Obligation Temporary Sales Tax Revenue Bonds

In 2000, the City authorized Temporary Sales Tax Revenue Bonds of \$17,925,000. The bonds are payable from revenues derived from the City's local 0.5% sales and use tax, and are backed by the full faith, credit, and taxing power of the City and are serviced by the Debt Service Fund.

General Obligation Sales Tax Revenue Note

In 2001, the City authorized the issuance of a \$2,500,000 General Obligation Sales Tax Revenue Note to finance the construction of transportation infrastructure improvements. As of December 31, 2001, no amounts have been advanced on this note.

General Obligation Revenue Bonds

General Obligation Revenue Bonds are recorded as liabilities in the Sewer Utility Enterprise Fund. The bonds are payable from revenues derived from the operation of the Sewer Utility Enterprise Fund and are backed by the full faith, credit and taxing power of the City.

Revenue Bonds

Revenue Bonds are recorded as liabilities in the Electric Utility Enterprise Fund. The bonds are payable from revenues derived from the operation of the Electric Utility Enterprise Fund.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 7: Long-Term Debt (Continued)

Notes Payable

The note payable recorded as a liability in the Electric Utility Enterprise Fund is payable from revenue derived from the operation of the Electric Utility Enterprise Fund.

The airport hangar notes payable are payable from airport hangar rental income.

Bond Indentures

There are a number of limitations and restrictions contained in the various bond indentures and note agreements and the City remains in substantial compliance with these requirements.

The following is a summary of the changes in long-term debt obligations for the year ended December 31, 2001:

	Balance 1/1/01	Additions	Retirements	Balance 12/31/01
<u>General Long-Term Debt</u>				
General Obligation Bonds:				
Tax Increment Bonds Series 1985	\$ 5,750,000		\$ 975,000	\$ 4,775,000
Taxable Tax Increment Bonds, District 7, Series 1997	2,669,380			2,669,380
Taxable Sales Tax Revenue Bond of 2000	9,700,000	\$758,673		10,458,673
Temporary Sales Tax Revenue Bonds, Series 2000A	17,925,000			17,925,000
Note Payable - Airport Hangar 1998	126,987		17,532	109,455
Note Payable - Airport Hangar 1999	166,256		18,473	147,783
Note Payable - Airport Hangar 2001		210,049		210,049
Total General Long-Term Debt	36,337,623	968,722	1,011,005	36,295,340
<u>Enterprise Funds</u>				
General Obligation Revenue Bonds:				
Wastewater Treatment Plant Refunding Bonds of 1992	8,875,000		8,875,000	
Wastewater Treatment Plant Refunding Bonds, Series 2001A		8,275,000		8,275,000
Revenue Bonds:				
Electric Utility Revenue Bonds, Series 2000	37,290,000		575,000	36,715,000
Other:				
Notes Payable	600,000		200,000	400,000
Total Enterprise Funds	46,765,000	8,275,000	9,650,000	45,390,000
Total	\$83,102,623	\$ 9,243,722	\$ 10,661,005	\$ 81,685,340

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 7: Long-Term Debt (Continued)

Changes in other long-term liabilities for the year ended December 31, 2001 are as follows:

	Balance 1/1/01	Increases	Decreases	Balance 12/31/01
<u>General Long-Term Debt</u>				
Accrued Compensated Absences	<u>\$ 4,940,322</u>	<u>\$ 3,219,756</u>	<u>\$ 2,948,334</u>	<u>\$ 5,211,744</u>

The annual requirements to amortize long-term debt obligations outstanding at December 31, 2001, excluding accrued compensated absences and including interest payments of \$38,702,269 over the life of the debt, are summarized below:

	General Obligation Revenue Bonds*	General Obligation Revenue Bonds	Revenue Bonds	Other	Total
2002	\$ 1,359,850	\$ 1,810,334	\$ 2,469,238	\$ 279,250	\$ 5,918,672
2003	1,392,125	19,329,150	2,470,738	268,130	23,460,143
2004	1,392,375	1,024,250	2,470,812	57,010	4,944,447
2005	1,437,750	1,012,300	2,469,462	57,010	4,976,522
2006		1,019,825	2,471,688	57,010	3,548,523
Thereafter		<u>5,053,740</u>	<u>59,175,272</u>	<u>182,237</u>	<u>64,411,249</u>
Totals	<u>\$ 5,582,100</u>	<u>\$ 29,249,599</u>	<u>\$ 71,527,210</u>	<u>\$ 900,647</u>	<u>\$ 107,259,556</u>

*Does not include the General Obligation Taxable Tax Increment Bonds, District No. 7, Series 1997 and the General Obligation Taxable Sales Tax Revenue Bond of 2000 which are structured without fixed principal maturities.

The City is subject to statutory limitation by the State of Minnesota for bonded indebtedness payable principally from property taxes. As of December 31, 2001, the City had not utilized any of its net legal debt margin which totaled \$90,917,168.

The City has issued several conduit debt obligations. These obligations do not constitute an indebtedness of the City and are not a charge against its general credit or taxing powers. The obligations are payable solely from revenues of the respective companies to which the proceeds were remitted. The original amount of the current issues totals \$1,149,758,000 and the balance outstanding at December 31, 2001 totals \$1,145,329,980.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 7: Long-Term Debt (Continued)

Pursuant to Minnesota Statutes (Section 273.74, Subd. 6) the City is required to disclose information related to its tax increment districts. These districts represent legal boundaries that allow the City to retain all incremental growth in assessed values.

District No.	Development District	Type of District	Date Created	Duration of District
2	2	Redevelopment	March 13, 1979	Through 2005
3-1	3	Redevelopment	February 14, 1988	25 Years following receipt of first increment
3-2	3	Housing	June 5, 1989	25 Years following receipt of first increment
5-1	5	Economic	June 6, 1994	11 Years or 9 Years following receipt of first increment, whichever is less
6-1	6	Housing	September 7, 1994	To February 1, 2014
7-1	7	Redevelopment	January 22, 1997	25 Years following receipt of first increment
8-1	8	Economic	April 7, 1997	11 Years from approval of TIF plan
10-1	10	Housing	January 20, 1999	25 Years following receipt of first increment
11-1	11	Housing	July 19, 1999	25 Years following receipt of first increment
12-1	12	Housing	August 16, 1999	25 Years following receipt of first increment
13-1	13	Housing	October 18, 1999	25 Years following receipt of first increment
14-1	14	Housing	November 1, 1999	25 Years following receipt of first increment
15-1	15	Housing	April 17, 2000	25 Years following receipt of first increment
16-1	16	Redevelopment	July 17, 2000	25 Years following receipt of first increment
17-1	17	Housing	September 6, 2000	25 Years following receipt of first increment
18-1	18	Housing	September 6, 2000	25 Years following receipt of first increment
19-1	19	Housing	September 6, 2000	25 Years following receipt of first increment
20-1	20	Housing	October 1, 2001	25 Years following receipt of first increment
21-1	21	Housing	October 15, 2001	25 Years following receipt of first increment
22-1	22	Housing	November 5, 2001	25 Years following receipt of first increment

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 7: Long-Term Debt (Continued)

Tax Increment District No. 2 was created pursuant to Minnesota Statutes Chapter 472A. All other Tax Increment Districts were created pursuant to Minnesota Statutes Chapter 469.

	Tax Increment District			
	<u>No. 2</u>	<u>No. 3-1</u>	<u>No. 3-2</u>	<u>No. 5-1</u>
Original net tax capacity	\$ 965,386	\$ 66,989	\$ 666	\$ 38,181
Current net tax capacity	3,913,622	181,203	9,808	111,424
Captured net tax capacity:				
Retained by authority	2,948,236	114,214	9,142	73,243
Shared with other taxing districts	-	-	-	-
Total general obligation tax increment bonds issued	23,678,300	-	-	-
Amounts redeemed	<u>18,903,300</u>	<u>-</u>	<u>-</u>	<u>-</u>
Outstanding bonds at December 31, 2001	<u>\$ 4,775,000</u>	<u>-</u>	<u>-</u>	<u>-</u>

	Tax Increment District		
	<u>No. 6-1</u>	<u>No. 7-1</u>	<u>No. 8-1</u>
Original net tax capacity	\$ 111	\$ 1,253	
Current net tax capacity	10,366	169,653	
Captured net tax capacity:			
Retained by authority	10,255	168,400	-
Shared with other taxing districts	-	-	-
Total general obligation tax increment bonds issued	-	2,669,380	-
Amounts redeemed	<u>-</u>	<u>-</u>	<u>-</u>
Outstanding bonds at December 31, 2001	<u>-</u>	<u>\$ 2,669,380</u>	<u>-</u>

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 7: Long-Term Debt (Continued)

	Tax Increment District				
	<u>No. 10-1</u>	<u>No. 11-1</u>	<u>No. 12-1</u>	<u>No. 13-1</u>	<u>No. 14-1</u>
Original net tax capacity	\$ 888	\$ 3,700	\$ 2,148	\$ 350	\$ 317
Current net tax capacity	7,738	11,953	28,632	463	317
Captured net tax capacity:					
Retained by authority	6,850	8,253	26,484	113	-
Shared with other taxing districts	-	-	-	-	-
Total general obligation tax increment bonds issued	-	-	-	-	-
Amounts redeemed	-	-	-	-	-
Outstanding bonds at December 31, 2001	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

	Tax Increment District				
	<u>No. 15-1</u>	<u>No. 16-1</u>	<u>No. 17-1</u>	<u>No. 18-1</u>	<u>No. 19-1</u>
Original net tax capacity	\$ 98	\$ 329	\$ 125	-	\$ 125
Current net tax capacity	98	329	125	-	125
Captured net tax capacity:					
Retained by authority	-	-	-	-	-
Shared with other taxing districts	-	-	-	-	-
Total general obligation tax increment bonds issued	-	-	-	-	-
Amounts redeemed	-	-	-	-	-
Outstanding bonds at December 31, 2001	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 7: Long-Term Debt (Continued)

	Tax Increment District		
	No. 20-1	No. 21-1	No. 22-1
Original net tax capacity	\$ 213	-	\$ 675
Current net tax capacity	213	-	675
Captured net tax capacity:			
Retained by authority	-	-	-
Shared with other taxing districts	-	-	-
Total general obligation tax increment bonds issued	-	-	-
Amounts redeemed	-	-	-
Outstanding bonds at December 31, 2001	-	-	-

NOTE 8: Reserved or Designated Fund Equity

Reserved fund equity represents the portion not available for expenditures or legally segregated for specific future use. Designated fund equity represents the portion which is based on tentative future spending plans. Fund equity has been reserved or designated at December 31, 2001 in the following funds:

General Fund

Reserved:	
Encumbrances	\$ 57,273
Prepaid items	7,107
Restricted assets	<u>23,473</u>
Totals	<u>\$ 87,853</u>
Designated:	
Subsequent years' appropriations	\$ 2,316,164
General contingency for future compensated absences	<u>4,196,731</u>
Totals	<u>\$ 6,512,895</u>

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 8: Reserved or Designated Fund Equity (Continued)

Special Revenue Funds

	<u>Library</u>	<u>Municipal Recreation</u>	<u>Totals</u>
Reserved:			
Encumbrances		\$ 28,441	\$ 28,441
Prepaid items	\$ 98		98
Restricted assets	95,340		95,340
Totals	<u>\$ 95,438</u>	<u>\$ 28,441</u>	<u>\$ 123,879</u>

Designated:

Subsequent years' appropriations	\$ 344,368	\$ 16,882	\$ 361,250
General contingency for future compensated absences	314,263	700,750	1,015,013
Totals	<u>\$ 658,631</u>	<u>\$ 717,632</u>	<u>\$ 1,376,263</u>

Debt Service Funds

	<u>Sales Tax Revenue Bonds</u>	<u>Tax Increment Bonds</u>	<u>Totals</u>
Reserved for Debt Service	\$ 2,606	\$ 450	\$ 3,056

Capital Project Funds

Reserved for encumbrances:			
Airport development			\$ 1,727,269
Park recreational and cultural development			456,067
Construction improvements			5,501,529
Reserved for interfund advances:			
Construction improvements			<u>3,886,681</u>
Totals			<u>\$ 11,571,546</u>

Enterprise Funds

Reserved for Debt Retirement:			
Sewer Utility			\$ 221,687
Electric Utility			2,471,688
Totals			<u>\$ 2,693,375</u>

Internal Service Funds

Reserved for Future Claims:			
Self-Insurance			<u>\$ 6,467,586</u>

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 9: Contributed Capital

Changes during 2001 in the contributed capital accounts of the Enterprise and Internal Service Funds are as follows:

<u>Enterprise Funds</u>	<u>Municipality</u>	<u>Capital Grants</u>	<u>Total Contributed Capital</u>
Balance beginning of year	\$ 22,646,118	\$ 22,064,804	\$ 44,710,922
Depreciation of assets acquired by capital grants		(1,333,756)	(1,333,756)
Balance end of year	<u>\$ 22,646,118</u>	<u>\$ 20,731,048</u>	<u>\$ 43,377,166</u>

<u>Internal Service Funds</u>	<u>Municipality</u>	<u>Capital Grants</u>	<u>Total Contributed Capital</u>
Balance beginning of year	\$ 3,825,646	\$ 26,874	\$ 3,852,520
Contribution of assets by other funds	8,659		8,659
Depreciation of assets acquired by capital grants		(2,511)	(2,511)
Balance end of year	<u>\$ 3,834,305</u>	<u>\$ 24,363</u>	<u>\$ 3,858,668</u>

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 10: Interfund Receivables, Payables and Transactions

The amounts due to and due from other funds as of December 31, 2001, at the individual fund level are summarized below:

Funds	Due from Other Funds	Due to Other Funds
General	\$ 617,760	\$ 171,474
Special Revenue:		
Library		10,592
Municipal Recreation System		140,009
Airport Operations		519,555
Capital Project:		
Airport Development	491,867	268,446
Community Development Projects		26,192
Tax Increment District		666,508
Construction Improvements	1,260,035	291
Enterprise:		
Parking		249
Electric Utility	501,292	1,570,328
Sewer Utility	674,877	150,988
Internal Service:		
Information Technology Revolving		21,199
Totals	\$ 3,545,831	\$ 3,545,831

The amounts advanced to and advanced from other funds as of December 31, 2001, at the individual fund level are summarized below:

	Advances to Other Funds	Advances from Other Funds
Special Revenue:		
Municipal Recreation System		\$ 1,958,931
Capital Project:		
Tax Increment District		1,927,750
Construction Improvements	\$ 3,886,681	
Totals	\$ 3,886,681	\$ 3,886,681

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 10: Interfund Receivables, Payables and Transactions (Continued)

Operating transfers during the year ended December 31, 2001 were as follows:

<u>Funds</u>	<u>Transfers In</u>	<u>Transfers Out</u>
General	\$ 518,071	\$ 2,067,269
Special Revenue	334,580	2,270,269
Debt Service	36,005	
Capital Project	5,378,794	1,092,789
Enterprise		767,097
Internal Service		70,026
Totals	<u>\$ 6,267,450</u>	<u>\$ 6,267,450</u>

NOTE 11: Segment Information for Enterprise Funds

Segment information from continuing operations for the year ended December 31, 2001 is as follows:

	<u>Parking Fund</u>	<u>Electric Utility Fund</u>	<u>Water Utility Fund</u>	<u>Sewer Utility Fund</u>	<u>Total Enterprise Funds</u>
Operating revenues	\$ 3,219,222	\$ 90,193,498	\$ 5,701,580	\$ 9,059,362	\$ 108,173,662
Depreciation expense	823,228	3,826,040	511,212	2,860,099	8,020,579
Operating income	344,467	4,037,557	1,472,792	782,854	6,637,670
Contribution in lieu of taxes	246,913	6,515,744	321,248	480,000	7,563,905
General property taxes				188,944	188,944
Intergovernmental revenues	577			48,742	49,319
Operating transfers out	17,097			750,000	767,097
Net income	707,117	5,980,064	1,554,708	632,947	8,874,836
Property Plant and Equipment					
Additions	723,584	30,425,429	1,066,096	1,573,198	33,788,307
Disposals	643,450	406,868	39,976	387,264	1,477,558
Net Working Capital	7,986,606	26,153,068	2,159,416	11,506,337	47,805,427
Total Assets	27,203,712	144,813,068	20,044,706	53,536,528	245,598,014
Bonds Payable		36,715,000		8,275,000	44,990,000
Total Equity	26,931,723	92,802,983	19,269,966	44,705,481	183,710,153

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 12: Employee Retirement Systems

The City participates in a statewide retirement plan administered by the Public Employees Retirement Association (PERA). PERA is the administrator of two cost-sharing multiple-employer retirement plans, the Public Employees Retirement Fund (PERF) and the Public Employees Police and Fire Fund (PEPFF). PERA issues a publicly available financial report that includes financial statements and required supplementary information for PERF and PEPFF. That report may be obtained by writing PERA, 60 Empire Drive #200, St. Paul, Minnesota 55103-1855 or by calling (651) 296-7460 or 1-800-652-9026. The following disclosures are made in accordance with Statement No. 27 of the Governmental Accounting Standards Board:

1. Cost-Sharing Multiple-Employer
Defined Benefit Pension Plans - Statewide
Public Employees Retirement Association

A. Plan Description

All full-time and certain part-time employees of the City of Rochester are covered by defined benefit plans administered by the Public Employees Retirement Association of Minnesota (PERA). PERA administers the Public Employees Retirement Fund (PERF) and the Public Employees Police and Fire Fund (PEPFF) which are cost-sharing multiple-employer retirement plans. These plans are established and administered in accordance with *Minnesota Statutes*, Chapters 353 and 356.

PERF members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security and Basic Plan members are not. All new members must participate in the Coordinated Plan. All police officers, fire-fighters and peace officers who qualify for membership by statute are covered by the PEPFF.

PERA provides retirement benefits as well as disability benefits to members, and benefits to survivors upon death of eligible members. Benefits are established by State Statute, and vest after three years of credited service. The defined retirement benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service.

Two methods are used to compute benefits for PERF's Coordinated and Basic Plan members. The retiring member receives the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate for a Basic Plan member is 2.2 percent of average salary for each of the first 10 years of service and 2.7 percent for each remaining year.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 12: Employee Retirement Systems (Continued)

A. Plan Description (Continued)

The annuity accrual rate for a Coordinated Plan member is 1.2 percent of average salary for each of the first 10 years and 1.7 percent for each remaining year. Under Method 2, the annuity accrual rate is 2.7 percent of average salary for Basic Plan members and 1.7 percent for Coordinated Plan members for each year of service. For PEPFF members the annuity accrual rate is 3.0 percent for each year of service. For all PEPFF members and for PERF members whose annuity is calculated using Method 1, a full annuity is available when age plus years of service equal 90. A reduced retirement annuity is also available to eligible members seeking early retirement.

There are different types of annuities available to members upon retirement. A normal annuity is a lifetime annuity that ceases upon the death of the retiree. No survivor annuity is payable. There are also various types of joint and survivor annuity options available which will reduce the monthly normal annuity amount, because the annuity is payable over joint lives. Members may also leave their contributions in the fund upon termination of public service, in order to qualify for a deferred annuity at retirement age. Refunds of contributions are available at any time to members who leave public service, but before retirement benefits begin.

The benefit provisions stated in the previous paragraphs of this section are current provisions and apply to active plan participants. Vested, terminated employees who are entitled to benefits but are not receiving them yet, are bound by the provisions in effect at the time they last terminated their public service.

B. Funding Policy

Minnesota Statutes Chapter 353 sets the rates for employer and employee contributions. These statutes are established and amended by the state legislature. The City makes annual contributions to the pension plans equal to the amount required by state statutes. PERF Basic Plan members and Coordinated Plan members are required to contribute 8.75% and 4.75% respectively, of their annual covered salary. PEPFF members are required to contribute 6.20% of their annual covered salary. The City of Rochester is required to contribute the following percentages of annual covered payroll: 11.43% for Basic Plan PERF members, 5.18% for Coordinated Plan PERF members, and 9.3% for PEPFF members. The City's contribution to the Public Employees Retirement Fund for the years ending December 31, 2001, 2000, and 1999 were \$1,507,888, \$1,432,489, and \$1,340,170, respectively. The City's contributions to the Public Employees Police & Fire Fund for the years ending December 31, 2001, 2000, and 1999 were \$1,138,078, \$1,058,736, and \$951,557, respectively. The City's contributions were equal to the contractually required contributions for each year as set by state statute.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 13: Deferred Compensation Plan

The City offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all City employees, permits them to defer a portion of their salary until future years. Participation in the plan is optional. The deferred compensation is generally not available to employees until termination, retirement, death, or unforeseeable emergency.

NOTE 14: Leases

The City is obligated under certain leases accounted for as operating leases. Operating leases do not give rise to property rights or long-term obligations and therefore the results of the lease agreements are not reflected in the City's account groups. Lease expenditures for the year ended December 31, 2001 totaled \$133,139.

Following is a schedule by years of future minimum rental payments required under operating leases that have remaining non-cancelable lease terms in excess of one year.

Years ending December 31:	
2002	\$ 29,745
2003	30,638
2004	31,557
2005	32,504
2006	33,479
Remaining lease terms	183,076

NOTE 15: Commitments and Contingencies

Contingencies:

General Litigation:

There are several pending lawsuits in which the City is involved. It is the opinion of management that substantially all of these claims would be covered by the liability insurance of the City and that potential claims against the City would not materially affect the financial statements.

Federally Assisted Programs:

The City participates in a number of federal agency assisted grant programs, principal of which are the Community Development Block Grant, Urban Mass Transportation, and Airport Development programs. These programs are subject to program compliance audits by the grantors or their representatives. The audits of certain programs for or including the year ended December 31, 2001, have not yet been completed. Accordingly, the City's compliance with applicable grant requirements will be established at some future date. The amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time although the City expects such amounts, if any, to be immaterial.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 15: Commitments and Contingencies (Continued)

Contingencies: (Continued)

Risk Management:

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City participates in the League of Minnesota Cities Insurance Trust (LMCIT) to provide its general liability and property coverage. The LMCIT is a public entity risk pool currently operating as a common risk management and insurance program for participating Minnesota cities. All cities in the LMCIT are jointly and severally liable for all claims and expenses of the pool. The amount of any liability in excess of assets of the pool may be assessed to the participating cities if a deficiency occurs. The City purchases commercial insurance for property values in excess of the LMCIT policy limits and all other risks of loss. Settled claims have not exceeded the LMCIT or commercial coverage in any of the past three fiscal years.

The City maintains a self-insurance program for employee group health coverage and worker's compensation. The City has established a Self-Insurance Fund (an internal service fund) to account for and finance its uninsured risks of loss. Under this program the Self-Insurance Fund provides coverage for up to a maximum of \$225,000 per group health claim (with a variable annual aggregate) and \$660,000 for each worker's compensation claim.

The City purchases commercial insurance for claims in excess of the coverage provided by the Self-Insurance Fund. All funds of the City participate in the program and make payments to the Self-Insurance Fund. The claim liability of \$2,334,276 reported in the Fund at December 31, 2001 is based on the requirements of Governmental Accounting Standards Board Statement No. 10, as amended by Governmental Accounting Standards Board Statement No. 30, which requires that a liability for claims be reported if information prior to the issuance of the financial statements indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated. Claim liabilities are based on the estimated ultimate cost of settling claims, including specific and incremental expenses, salvage, and subrogation. The claim liability does not include other allocated or unallocated claim adjustment expenses.

CITY OF ROCHESTER, MINNESOTA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2001

NOTE 15: Commitments and Contingencies (Continued)

Contingencies: (Continued)

Changes in the Fund's claims liability amount during the years ended December 31, 2001 and 2000 were as follows:

<u>Year Ended</u>	<u>Beginning of Year Liability</u>	<u>Current Year Claims and Changes to Estimates</u>	<u>Claim Payments</u>	<u>End of Year Liability</u>
2001	\$ 1,948,055	\$ 6,688,928	\$ (6,302,707)	\$ 2,334,276
2000	1,752,298	4,755,033	(4,559,276)	1,948,055

Commitments:

Rochester Public Utilities ("Utility") has entered into a power purchase agreement with Southern Minnesota Municipal Power Agency ("Agency"). Under the terms of the agreement the Agency provided virtually all Utility power requirements through 1999. In 1999, the Utility and SMMPA agreed to a contract rate of delivery (CROD) beginning in 2000. The CROD caps the amount of power SMMPA must supply to the Utility under the power purchase contract. The Utility is responsible for acquiring its power needs above the CROD. The contract expires in the year 2030.

In 1992 Rochester Public Utilities ("Utility") entered into an agreement with the Minnesota Municipal Power Agency ("MMPA") to sell a maximum of 100 megawatts of power annually to MMPA beginning July 1, 1995, at a fixed rate. Under the terms of the agreement, the Utility is paid a fixed fee for providing the availability of generating capacity and is reimbursed for the fuel-related costs of generating power.